Supreme Court, U.S.
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No. 99-2025

In The

Supreme Court of the United States

EDDIE EDWARDS,

Petitioner,

v.

WALTER JONES CONSTRUCTION, THE CITY OF OBERLIN, OHIO PUBLIC WORKS COMMISSION, MICHAEL SIGG, MELVIN GRAVELY,

Respondents.

On Petition For Writ Of Certiorari To The United States Court Of Appeals For The Sixth Circuit

RESPONDENTS, THE CITY OF OBERLIN AND MICHAEL SIGG'S, BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

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QUESTIONS PRESENTED

Whether a shareholder suing in his own name has standing to assert the claims of a corporation under 42 U.S.C. § 1981 or 42 U.S.C. § 1983.

Whether a federal court of appeals may determine a violation of its local rules has occurred, that an appeal is frivolous, and an award of attorney fees as a sanction.

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STATEMENT OF THE CASE

Petitioner and Plaintiff Eddie Edwards, the sole shareholder of EENSC, Inc., an Ohio Corporation, personally and individually filed suit against the Walter Jones Construction Company (WJCC) and several Ohio government entities and officials including the City of Oberlin. Edwards alleged violations of 42 U.S.C. §§ 1981 and 1983 in connection with the putative breach of a contract between EENSC and WJCC.

The District Court dismissed Edwards' complaint on several grounds, among which was that Edwards, as a shareholder, in his personal capacity lacked standing to assert the corporation's claims. The decision was upheld by the Appeals Court, without comment on the alternative bases for dismissal.

The Court of Appeals granted WJCC's motion for attorney fees first, because Edwards presented arguments in his "final" brief that he had not included in his "proof" brief in violation of Sixth Circuit rule 28(a), and second, on the basis that Edwards frivolously asserted standing without presenting a nonfrivolous argument for the modification or reversal of existing law as required by Rule 11 of the Federal Rules of Civil Procedure. Edwards now petitions this Court for A Writ of Certiorari based upon purported errors by the lower court in denying standing and in awarding the Respondent sanctions under Rule 11.

SUMMARY OF ARGUMENT

I. A corporation has standing to pursue a claim based on 42 U.S.C. § 1981 or 42 U.S.C. § 1983. A sole shareholder of the corporation may not usurp the standing of the corporation by asserting the corporation's claims.

II. The federal court of appeals may sanction counsel for the breach of the circuit's local rules where counsel posits a new argument in the final brief which did not appear in the earlier proof brief. In addition, the court of appeals is able to determine whether an assignment of error is frivolous.

ARGUMENT

I. The Petitioner lacks standing to sue in his individual capacity for injuries allegedly inflicted upon his wholly owned corporation.

While a plaintiff must fulfill Article III's "case or controversy" requirement in order to maintain standing to sue in an Article III court, additional "prudential" limitations on standing may exist. *Warth v. Seldin*, 422 U.S. 490, 498-500 (1975). Among these limitations is that a litigant must assert his own interests, as opposed to those of third parties. *Phillips Petroleum Co. v. Shutts*, 472 U.S. 797, 804 (1985). Consistent with this premise, Federal Rule of Civil Procedure 17(a) specifies that "Every action shall be prosecuted in the name of the real party in interest."

A Corporation is considered to be a person under the law, who can sue and be sued, cannot be denied liberty or property without due process of law, and falls within the ambit of the Equal Protection Clause of the Fourteenth Amendment. *First Nat'l Bank of Boston v. Bellotti*, 435 U.S. 765, 780 n.15 (1978); *Wheeling Steel Corp. v. Glander*, 337 U.S. 562, 574 (1949) (Jackson, J., addendum); *Grosjean v. American Press Co.*, 297 U.S. 233, 244 (1936); *Liggett Co. v. Baldridge*, 278 U.S. 105, 111 (1928), *overruled by North Dakota Pharmacy Bd. v. Snyder's Drug Stores, Inc.*, 414 U.S. 167 (1973) *on other grounds*; *Minneapolis Ry. v. Beckwith*, 129 U.S. 26, 28, 29 (1989); *Santa Clara County v. Southern Pac. R.R.*, 118 U.S. 394 (1886). Thus, it has generally been held that a shareholder, in his or her personal capacity, lacks standing to enforce the claims of a corporation for professed wrongs to it.

In order to have standing, the shareholder must allege an injury separate and distinct from that of the corporation. It is upon this independent injury that the shareholder's claims must be based. *Werner Frank v. Hadesman and Frank, Inc.*, 83 F.3d 158, 160 (7th Cir. 1996); *Arent v. Distribution Sciences, Inc.*, 975 F.2d 1370, 1373, 1374 (8th Cir. 1992); *Williams v. Mordkofsky*, 901 F.2d 158, 164 (D.C. Cir. 1990); *Searcy v. Houston Lighting & Power Co.*, 907 F.2d 562, 565 (5th Cir. 1990); *Gaff v. Federal Deposit Insurance Corporation*, 814 F.2d 311, 315 (6th Cir. 1987). This is true even when the plaintiff(s) is (are) the sole shareholder(s) in the corporation. *Soranno's Gasco, Inc. v. Morgan*, 874 F.2d 1310 (9th Cir. 1989); *Canderm Pharmacal, Ltd. v. Elder Pharmaceuticals, Inc.*, 862 F.2d 597, 603 (6th Cir. 1988); *Schaffer v. Universal Rundle Corporation*, 397 F.2d 893, 896 (5th Cir. 1968); *Erlich v. Glasner*, 418 F.2d 226,

228 (9th Cir. 1969). It is also true for lawsuits filed under Federal civil rights statutes. *Searcy*, 907 F.2d at 562; *Soranno's Gasco, Inc.*, 874 F.2d at 1318; *Flynn v. Merrick*, 881 F.2d 446, 450 (7th Cir. 1989); *Smith v. Martin*, 542 F.2d 688, 690 (6th Cir. 1976); *Glasner*, 418 F.2d at 228. To hold otherwise would create a risk of double recovery, *Vinci v. Waste Management, Inc.*, 80 F.3d 1372, 1375 (9th Cir. 1996), multitudinous litigation, and would disregard the corporate entity. *Glasner*, 418 F.2d at 228.

Moreover, there exists a presumption that state law should be incorporated into federal common law unless the application of state law conflicts with a specific objective of a federal program. *Kamen v. Kemper Fin. Serv., Inc.*, 500 U.S. 90, 98 (1991). Since corporation law is in the main an issue of state law, the laws of Ohio with regard to standing to assert the claims of corporations should govern. Ohio follows the general rule that a shareholder has no cause of action against third parties for injury to the corporation in which he owns shares, unless the shareholder has sustained a direct injury that is distinct from that of the corporation. *Adair v. Wozniak*, 492 N.E.2d 426, 429 (Ohio 1986).

The Petitioner cites a number of cases that purportedly support his standing claim. However, none of these is apposite to the case at bar. In each of the cases referenced by the Petitioner, the plaintiffs had claims upon the defendants that were separate and distinct from the potential claims of the corporations in which the plaintiffs were shareholders. Conversely, the Petitioner in the instant case alleges only claims that accrue to, and are derivative through, his corporation.

In *Hunter v. Old Ben Coal Co.*, 844 F.2d 428 (7th Cir. 1988) former shareholders of a dissolved Illinois not-for-profit corporation brought suit against a Delaware corporation seeking specific performance of an option contract that obligated the Defendant to acquire the former shareholders' coal interests. At issue was whether or not the Plaintiffs' claims were time barred by an Illinois corporate survival statute applicable to not-for-profit corporations. In reversing the District Court, the Seventh Circuit Court of Appeals held that the corporate survival statute was inapplicable because *the Plaintiffs' claims were personal, and not derivative,* in nature. Specifically, the Court found that the Plaintiffs were "direct" beneficiaries, and therefore third-party beneficiaries, of the contract, to whom the Defendant owed a direct duty.

Buschmann v. Professional Men's Association, 405 F.2d 659 (7th Cir. 1969), cited by the Plaintiffs, is likewise inapposite to the case at bar. In *Buschmann*, the Plaintiff, C. Severin Buschmann, Jr., was a party to a contract in which Buschmann, a shareholder, guaranteed the debt of a corporation in his personal capacity. Although the corporation also had a cause of action against the Defendant corporation for mismanagement that resulted from the same wrongful acts, Buschmann's claims were personal because promises were made directly to him in his individual capacity, and it was the breach of these promises which gave rise to his cause of action. Buschmann's liability to pay the corporation's indebtedness, which was the central issue upon which his claim for damages were based, was an independent, individual obligation that did not arise from his shareholder status.

In *Eden v. Miller*, 37 F.2d 8 (2nd Cir. 1930), the Plaintiffs contracted directly with the Defendants, and sought to recover their personal damages, not those of the corporation of which they were shareholders. *Jones v. Int'l Union of Operating Eng'rs*, 603 F.2d 664 (7th Cir. 1979), involved a suit by union members against their union, and did not address the rights of shareholders to sue independently for wrongs to a corporation. The United States Court for the District of Puerto Rico, in *W. Clay Jackson Enters., Inc. v. Greyhound Leasing & Fin. Corporation*, 463 F.Supp. 666 (D. P.R. 1979), did find that stockholders in a close corporation could assert claims such as loss of credit, business reputation, and emotional distress *that were distinct and separate from the claims of the corporation*. However, the Court followed the general rule that shareholders cannot maintain actions to redress injuries to a corporation, and dismissed the Plaintiffs' claims for diminution in the value of their corporate investments. *Id.* at 670-671.

Crosby v. Beam, 548 N.E.2d 217 (Ohio 1989), cited by the Petitioner, held that a minority shareholder in a close corporation may on his or her own behalf sue the majority shareholder(s) for breach of the fiduciary duty she or he is owed. This exception to the general rule regarding shareholder actions is confined to the enforcement of minority shareholders' rights vis-a-vis majority shareholders, and creates no individual shareholder cause of action against third parties alleged to have injured a corporation. *Id.* at 221.

On pages 7 and 8 of his Petition, Edwards cites several cases dealing with proper claims and pleading standards under 42 U.S.C. §§ 1981 and 1983. Yet none of

these cases supports the contention that an individual shareholder is the proper party in a lawsuit that seeks to enforce a corporation's civil rights claims against third parties. Petitioner cites *German v. Killeen*, 495 F.Supp. 822, 827 (E.D. Mich 1980), for the proposition that "To invoke the protection of § 1981, plaintiff must establish that . . . he was unable to make or enforce a contract that a white person could make or enforce." (Edwards' Petition for Certiorari at 7.) This point is uncontested. However, EENSC was the contracting party in the case at bar, not Edwards. Edwards was neither a party to the contract in dispute, nor a direct beneficiary of said contract other than as a shareholder of EENSC. Consequently, any suit based on claims of this contract must be brought by EENSC on its own behalf.

Leatherman v. Tarrant County Narcotics and Intelligence & Coordination Unit, 507 U.S. 163 (1993), cited by Edwards on page 8 of his Petition, held that a federal court may not apply a "heightened pleading standard" in civil rights cases alleging municipal liability under 42 U.S.C. § 1983. The case does not address the issue of the proper party in a civil rights lawsuit where injury to a corporation is alleged. Therefore, *Leatherman* fails to support Edwards' petition.

The Court of Appeals was correct in affirming the District Court's ruling that the Petitioner in the case at bar lacked standing to sue on behalf of his corporation. Consequently, certiorari should be denied.

II. The Court of Appeals was justified in imposing sanctions upon the Petitioner for wilful disregard of a Court rule and for his frivolous assertion of standing to sue on behalf of his corporation.

The imposition of attorney fees as a sanction is well within the power of the Federal Courts. *Chambers v. Nasco, Inc.*, 501 U.S. 32 (1991). By presenting a document to a federal court, an attorney certifies that the claims and legal arguments made therein are "warranted by existing law or by a nonfrivolous argument for the extension, modification, or reversal of existing law or the establishment of new law . . . " Fed. R. Civ. P. 11(b)(2).

Edwards wilfully disregarded Sixth Circuit Rule 28(a), which provides for the filing and service of "proof" and "final" briefs, the proof briefs to contain all legal arguments presented without modification. Instead, Edwards introduced an entirely new argument in his final brief. Edwards chose to ignore Rule 28(a) despite having obtained three extensions beyond the initial briefing deadlines for the appeal.

Although it is well settled that a shareholder may not, in his or her individual capacity, sue to enforce the rights of a corporation in which he owns stock, Edwards has argued that by virtue of his status as a shareholder he is a "third party beneficiary" of contracts into which the corporation entered. In this assertion, Edwards has failed to advocate "a nonfivolous argument for the extension, modification, or reversal of existing law or the establishment of new law." Consequently, this Court should deny Certiorari to the Petitioner.

CONCLUSION

The Petitioner, the sole shareholder of a wholly owned corporation, argues that the District Court and Sixth Circuit Court of Appeals were in error in denying him standing to sue third parties for alleged injuries sustained by the corporation, although he, himself, did not personally claim a separate and distinct injury. He further appeals an award of sanctions to the opposing party. Sanctions were awarded both because the Petitioner violated Sixth Circuit rules by adding an additional argument to his final brief after his proof brief had been filed and served, and because he presented a frivolous argument to a federal court.

The lower court decisions were in keeping with the general rule regarding lawsuits by corporate shareholders, and consistent with the laws of Ohio, the governing jurisdiction. The award of sanctions was soundly within the discretion of the Appeals Court.

This case does not present a split between the governing law of different circuits, nor is it a decision that represents a significant conflict between state supreme courts, or a state court of last resort and a United States Court of Appeals. The Sixth Circuit's decision is in accordance with prior precedent, and involves no compelling

issues that need be decided by this Court. Certiorari should, therefore, be denied.

Respectfully submitted,

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